Fact Sheet
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The Democratic Alternative Tax Plan

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The Senate tax bill is much improved from the House bill. The Finance Committee worked in a bipartisan manner, giving Democratic Senators significant input. Nevertheless, it remains skewed in favor of wealthier taxpayers and features a variety of backloaded provisions that will make it more difficult to keep the Federal budget balanced after 2002.

Senate Democrats sought further improvements on the floor and proposed an alternative tax bill. The Democratic Alternative:

- is fairer to working families with children;
- targets its growth incentives to encourage new investment;
- offers more help for education; and,
- is more fiscally responsible.

Family Tax Relief

The bill includes a per-child tax credit that is refundable against both income taxes and payroll taxes, and is calculated before a taxpayer's Earned Income Tax Credit (EITC). The refundability and EITC stacking would improve the Senate bill by making the per-child credit applicable to millions more children. The Senate bill's provision would not apply to most children whose parents make less than $25,000 per year. Many of those taxpayers do not pay enough income tax to benefit from the credit, but have a heavy Federal tax burden. In this way, the Democratic alternative provides payroll tax relief, a tax cut neither the House or Senate tax bills offer American families.

Encouraging saving

The alternative would give parents an incentive to save for their children's future by providing $500 per child if the money is invested in an IRA for the child and $350 otherwise. The funds could be withdrawn without penalty if used for the child's higher education.

Democratic Policy Committee
United States Senate
Washington, D.C., 20510-7050

Tom Daschle, Chairman
Harry Reid, Co-Chairman

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Tax Incentives for Education and Training

The Democratic alternative aims to provide tax cuts to help families pay for higher education expenses and provide more help to the people who need it most.

More help with education costs. The alternative includes $47 billion in education tax cuts over five years, nearly $15 billion more than the Senate bill. It includes $37.3 billion in education cuts modeled on the President's proposals while the Senate bill provided only $20.4 billion for those cuts, nearly $15 billion below the level in the bipartisan budget agreement.

HOPE credit. The alternative includes a full tax credit for the first $1,000 of tuition expenses, then a 50 percent credit for additional expenses up to the credit's limit, which is $1,100 in 1997-99, $1,200 in 2000 and $1,500 thereafter.

The HOPE credit helps with the first two years of college. For the next two years, the alternative includes a tax credit of 20 percent of higher education expenses, limited to $800 in 1997-1999, $1,500 in 2000 and $2,000 thereafter.

Employer-provided education assistance. The alternative permanently extends this exclusion for both undergraduate and graduate courses.

Student loan interest. It allows for an annual deduction of up to $2,500 for student loan interest payments.

School construction. The alternative establishes a tax credit program to help school districts repair, renovate, modernize or construct elementary and secondary school facilities.

Family Savings and Business Capital Formation

A fair capital gains cut. Current law gives taxpayers in the highest bracket the equivalent of a 30 percent exclusion for capital gains. Instead of giving higher-income taxpayers an even bigger break, the Democratic alternative would give all taxpayers the same 30 percent exclusion for assets held three years or longer.

Beginning in 2003, the alternative would also allow the exclusion for the first $500 per year in stock dividends, an investment incentive not included in the Senate or House bill.

In addition, up to $500,000 in capital gains profit on the sale of a home would be tax-free. Finally, the alternative provides a 50 percent capital gains exclusion on the sale of small business corporate stock, including interests in partnerships, S corporations, and sole proprietorship. This additional exclusion expands a capital gains cut Democrats enacted in 1993, so it will help encourage investment in more small businesses and farms.

Targeting tax relief. These proposals would focus the investment incentives toward Main Street, not Wall Street. Middle-income investors would get the same breaks as the wealthy. They are more likely to respond to a tax incentive with new investment. Tax incentives for wealthier investors are likely to be less efficient and give many a windfall for investments they would make regardless of the new tax cuts. Limited resources are available to encourage investment within a balanced budget plan—the Democratic alternative's more targeted approach makes better use of those resources.

Estate Tax Relief for Family Businesses and Farms

The alternative exempts the first $900,000 in a family-owned business or farm from estate taxation. That would allow at least $1.5 million (at least $2.1 million if a spousal exemption applies) of a family business or farm to be passed along to the next generation without tax. For larger family farms and businesses, up to $2.5 million in estate taxes could be paid over time, at below-market interest rates.

Miscellaneous Provisions

The alternative includes a variety of miscellaneous provisions, many of which are in the Senate bill or the President's budget. These include:

- extensions of the expiring research, Welfare-to-work, and contribution of appreciated stock provisions, as well as a permanent orphan drug credit;
- alternative minimum tax relief for individuals;
- District of Columbia tax incentives;
- Brownfields tax incentives for environmental cleanup in distressed communities;
- an expanded Empowerment Zone and Enterprise Community program;
- Foreign Sales Corporation benefits for computer software;
- a 100% deduction of health insurance premiums for the self-employed;
- a package of pension simplification proposals; and,
- an end to the "spousal link" that restricts a taxpayer's ability to contribute to an IRA if their spouse has access to a pension plan at work.

In addition, the Democratic Alternative would retain all the revenue offsets included in the bill reported by the Senate Finance Committee.